

AMENDED IN SENATE APRIL 29, 2004

AMENDED IN SENATE MARCH 22, 2004

SENATE BILL

No. 1406

Introduced by Senator Ackerman

February 18, 2004

An act to amend Section 25118 of the Corporations Code, relating to usury.

LEGISLATIVE COUNSEL'S DIGEST

SB 1406, as amended, Ackerman. Usury exemption.

The California Constitution prohibits usury, which is the loan or forbearance of any money, goods, or things at a rate of interest in excess of specified rates, but exempts certain transactions and lenders from these provisions, and allows the Legislature to exempt additional classes of person by statute. Existing statutory law, the Corporate Securities Act of 1968, exempts certain evidences of indebtedness issued by an entity with total assets of at least \$2,000,000 from the usury provisions of the California Constitution and exempts certain evidences of indebtedness in an amount of at least \$300,000 from those usury provisions under certain circumstances.

This bill would require that both of the above requirements be satisfied for these evidences of indebtedness to be exempt from the usury provisions of the California Constitution. The bill would provide that this exemption from the usury provisions of the California Constitution would be available only to a person who is in compliance with *either* the California Finance Lenders Law *or the Real Estate Law*.

Vote: majority. Appropriation: no. Fiscal committee: no. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 25118 of the Corporations Code is amended to read:

25118. (a) An evidence of indebtedness issued by an entity or guaranteed by an entity that is an affiliate (as defined in Section 150) of the borrower that, on the day the evidence of indebtedness issued or guaranty is first issued or entered into, has total assets of at least two million dollars (\$2,000,000) according to its then most recent financial statements, and the purchasers or holders thereof, shall be exempt from the usury provisions of the California Constitution if the provisions of this subdivision and subdivision (b) are satisfied. The financial statements referred to in the preceding sentence shall meet both of the following requirements:

(1) Be as of a date not more than 90 days prior to the date the evidence of indebtedness or guaranty is first issued or entered into.

(2) Be prepared in accordance with either of the following:

(A) In accordance with generally accepted accounting principles and, if the entity has consolidated subsidiaries, on a consolidated basis.

(B) In accordance with the rules and requirements of the Securities and Exchange Commission, whether or not required by law to be prepared in accordance with those rules and requirements.

(b) Any one or more evidences of indebtedness, and the purchasers or holders thereof, shall be exempt from the usury provisions of the California Constitution if either of the following applies and the provisions of this subdivision and subdivision (a) are satisfied:

(1) The evidences of indebtedness aggregate at the time of issuance at least three hundred thousand dollars (\$300,000) in original face amount, or, if the evidences of indebtedness are purchased with original issue discount, they are purchased for an aggregate purchase price at the time of issuance of at least three hundred thousand dollars (\$300,000).

(2) The evidences of indebtedness are issued pursuant to a bona fide written commitment for the lending to the issuer of at least three hundred thousand dollars (\$300,000), or the provision of a line of credit to the issuer in a principal amount of at least three hundred thousand dollars (\$300,000). The exemption provided by

1 this paragraph shall not be affected by a subsequent event of
2 default or other event not in the lender's control that has relieved
3 or may relieve the lender from its commitment.

4 (c) Any evidence of indebtedness described *in* subdivisions (a)
5 and (b), and the purchasers or holders thereof, shall be entitled to
6 the benefits of the usury exemption contained in this section
7 regardless of whether, at any time after the evidence of
8 indebtedness or guaranty upon which the exemption is based is
9 first issued or entered into, the evidence of indebtedness or
10 guaranty is determined by a court of competent jurisdiction not to
11 be a "security."

12 (d) This section creates and authorizes a class of transactions
13 and persons pursuant to Section 1 of Article XV of the California
14 Constitution.

15 (e) This section does not apply to:

16 (1) Any evidence of indebtedness issued or guaranteed (if the
17 guaranty is part of the consideration for the indebtedness) by an
18 individual, a revocable trust having one or more individuals as
19 trustors, or a partnership in which, at the time of issuance, one or
20 more individuals are general partners.

21 (2) Any transaction subject to the limitation on permissible
22 rates of interest set forth in paragraph (1) of the first sentence of
23 Section 1 of Article XV of the California Constitution.

24 (f) The exemptions created by this section shall only be
25 available in a transaction that meets either of the following criteria:

26 (1) The lender and either the issuer of the indebtedness or the
27 guarantor, as the case may be, or any of their respective officers,
28 directors, or controlling persons, or, if any party is a limited
29 liability company, the managers as appointed or elected by the
30 members, have a preexisting personal or business relationship.

31 (2) The lender and the issuer, or the lender and the guarantor,
32 by reason of their own business and financial experience or that of
33 their professional advisers, could reasonably be assumed to have
34 the capacity to protect their own interests in connection with the
35 transaction.

36 (g) For purposes of this section, "preexisting personal or
37 business relationship" and "capacity to protect their own interests
38 in connection with the transaction" as used in subdivision (f) shall
39 have the same meaning as, and be determined according to the
40 same standards as, specified in paragraph (2) of subdivision (f) of

1 Section 25102 and its implementing regulations provided that,
2 solely with respect to this section, a lender or purchaser who is
3 represented by counsel may designate that person as its
4 professional adviser whether or not that person is compensated by
5 the issuer or guarantor, as long as that person has a bona fide
6 attorney-client relationship with the lender or purchaser.

7 (h) ~~This~~ *The exemptions created by this section shall not apply*
8 ~~to a person who is not~~ *only be available to a person who is in*
9 *compliance with the California Finance Lenders Law (Division 9*
10 *(commencing with Section 22000) of the Financial Code) or the*
11 *Real Estate Law (Division 4 (commencing with Section 10000) of*
12 *the Business and Professions Code).*

